

Single Electricity Market Committee

Curtailment Approach on SEM Interconnectors

Decision Paper

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1. Introduction

In September 2011, pursuant to their respective interconnector licences granted by NIAUR, CER and Ofgem the interconnector owners (EirGrid Interconnector Limited and Moyle Interconnector Limited) consulted upon and submitted Access Rules to the SEM Committee. Co-ordinated Access Rules were approved by the respective regulators (Ofgem and SEM Committee) for the Moyle and East West Interconnector (EWIC) and these Access Rules came into effect in October 2011. These Access Rules were developed in accordance with EU legislation¹ and aligned as far as possible, and in particular regarding material matters, with the Access Rules of other FUI Interconnectors.

In September 2012 an amended version of the Access Rules was approved by the respective regulators to reflect changes consequent upon the introduction of intra-day trading in SEM.

In approving this amended version of the Access Rules for the East West Interconnector² and the Moyle Interconnector³ in 2012, the respective Regulators requested that a review and consultation dealing with capacity auction management and the curtailment of capacity on the SEM Interconnectors be undertaken on a joint basis by the EWIC and Moyle Interconnector Owners. The Regulators requested that two issues be addressed as part of this review.

1. To consider whether, in the event of reduced availability, the practice of auctioning (in future auctions) only the capacity which is forecast to be available was the correct approach and was in accordance with Regulation (EC) No. 714/2009 (the Regulation).
2. To consider precisely how already allocated capacity would be curtailed in the event of an outage. It was noted that both the EWIC Access Rules and the Moyle Access Rules are silent on this presently. Current practice dictates that all Modified Interconnector Nominations are reduced on a pro-rata basis.

The remainder of this paper deals with the issues raised in the Interconnector Owners' *Report on the Curtailment Approach*, (the Report) published on 13 November 2012; the responses from participants to the Report, the recommendations of the Interconnector Owners; and concludes with the SEM Committee's Decision. It is recommended that the Interconnector Owners' recommendations be read in conjunction with this paper. It should also be noted that the views in this paper attributed to SEM RAs have been discussed with Ofgem.

¹ Regulation (EC) No. 714/2009 Annex I paragraph 3.2

² EWIC Access Rules – <http://www.eirgrid.com/media/East%20West%20Interconnector%Access%20Rules%20-%20approved%20September%202012.pdf>

³ Moyle Access Rules – <http://www.mutual-energy.com/Download/120821%20Moyle%20Interconnector%20-%20Access%20Rules.pdf>

2. Management of Auction Capacity on the SEM interconnectors

2.1. Current Approach

The current Access Rules for Moyle and EWIC outline how transfer capacity on the interconnectors is auctioned in long-term and daily auctions and how the volume of capacity put up for auction is based on forecast availability. Rules D3.3 and D4.3 state:

“D3.3: The number of Units auctioned in a Long Term Auction will include:

- (a) A proportion (as determined by the Operator) of the available Interconnector Capacity (in the form of Units) not already allocated to Users; and
- (b) Resale Units (if any) made available for Resale at such Long Term Auctions pursuant to Rule E4 [Secondary Market]

D4.3 The total Offered Capacity for any Trading Day in Daily Auctions will include:

- (a) **Available Interconnector Capacity** (in the form of Units) **not already allocated** to Users **and that is not unavailable due to Outages** and/or due to the application of Curtailment;
- (b) Unused Units (if any) that have become available for the Daily Auctions pursuant to Rule E4 [Secondary market] or Rule E5 [UIOSI] and that are not unavailable due to Outages and/or due to the application of Curtailment.(emphasis added)”

The first issue the RA’s requested be addressed as part of the 2012 review of the Access Rules was whether the current approach in auction capacity management, i.e. to auction only the capacity that is forecast to be available, was the correct approach and was in accordance with Regulation (EC) No. 714/2009 (the Regulation)⁴⁵. The Regulation states: “[e]ach capacity-allocation procedure shall allocate *a prescribed fraction of the **available interconnection plus any remaining capacity not previously allocated and any capacity released by capacity holders from previous allocations.***” (Emphasis added in bold)

2.2. Interconnector Operator Consultation

A *Report on the Curtailment Approach* (the Report) was published on 13 November 2012 by the Interconnector Operators. The Report aimed to provide information on the treatment of Interconnector capacity in the event of curtailment and on capacity auction

⁴ Regulation (EC) No 714/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the network for cross-border exchanges in electricity and repealing Regulation (EC) No 1228/2008

⁵ Regulation (EC) No 714/2009

management across the FUI region. Responses to the Report were elicited from Market Participants. Six parties responded⁶. The RAs sought clarification on a number of issues from the Interconnector Owners and their response was received on 5 April 2013. The Interconnector Owners' response to that request for clarification will be published with this Decision Paper.

2.3. Summary of Responses

Five of the six respondents agreed with the current approach to capacity auction management, where capacity auctions are not held for capacity over and above the forecast available interconnection capacity. These five respondents believed that the current approach is in accordance with the Regulation. One respondent stated that any sale of capacity above that forecast to be available at the time of the auction would contravene the objective of the Regulation. Another mentioned that, once a curtailment has occurred, it would be contrary to Article 16(3) of the Regulation to continue to allocate capacity in excess of the forecast availability since it would be beyond the level compatible with secure system operation.⁷ Furthermore, value was placed on the fact that the current approach regarding the auctioning of capacity ensured that the FUI region was fully aligned on this matter.

However, one respondent was unequivocal in their view that the current practice on Moyle and EWIC is not in line with the Regulation (with particular reference to paragraph 2.7 of the Congestion Management Guidelines).⁸ They suggest that the auctioning policy appears to directly discriminate against one class of interconnector users – namely shorter term purchasers of capacity – in favour of longer term purchasers of capacity. In particular they state shorter term purchasers of capacity suffer the vast majority of the outage risk whilst the long term purchasers take very little. This respondent would have preferred to see all auctions held irrespective of available interconnection capacity and to apply the pro-rata reductions to all capacities held afterward. This respondent supported their argument by presenting an interpretation of the Regulation which differs from that of the interconnector operators.

2.4. Recommendation of the Interconnector Owners

The Interconnector Owners are satisfied that the approach taken in the Access Rules is fully in accordance with the Regulation. They commented that there was strong support from

⁶ Six parties responded to the consultation not including the Interconnector Owners. As a number of the responses were submitted confidentially, respondents' identities have been protected for the purpose of this Decision Paper.

⁷ Article 16(3) of the Regulation reads: *The maximum capacity of the interconnections and/or the transmission networks affecting cross-border flows shall be made available to market participants, complying with safety standards of secure network operation.*

⁸ Para. 2.7. of Annex I to Regulation (EC) No. 714/2009 reads: *Capacity allocation shall not discriminate between market participants that wish to use their rights to make use of bilateral supply contracts or to bid into power exchanges. The highest value bids, whether implicit or explicit in a given timeframe, shall be successful.*

respondents regarding the Interconnector Owners' compliance with EU Regulations and the continued practice of auctioning only forecast available capacity and not auctioning capacity that is unavailable owing to the application of curtailment. They acknowledged that this was an important area for alignment with other Interconnectors across the FUI region.

The Interconnector Owners stated that they auction their forecast available capacity and do not auction capacity that was unavailable due to curtailment, in accordance with their approved Access Rules. The cancellation of shorter term auctions where interconnector capacity was not available in order to honour already allocated capacity contracts does not in their view represent discrimination between market participants that wished to use their rights to make use of bilateral supply contracts or to bid into power exchanges. According to the Interconnector Owners, how users intend to use interconnector capacity was irrelevant to the capacity allocation process and capacity that was allocated in long or short term auctions may be used in either way.

2.5.SEM Committee Decision

The SEM Committee is of the view the reference in the Regulation to “[.] any remaining capacity not previously allocated and any capacity released by capacity holders from previous allocations”⁹ suggests that ‘available’ in this context means forecast available capacity;

Condition 15 of the EWIC’s Electricity Interconnector Operator Licence together with Article 16(3) of Regulation (EC) 714/2009 require that the Interconnector Operator “*make available the maximum capacity of the Licensee’s Interconnector, in compliance with safety standards of secure network operation and as set out in the Regulation (EC) 714/2009 [.]*” Therefore, the obligation is to make available (i.e. to auction) the maximum capacity that is physically available taking due account of outages, including scheduled outages, needed to provide system security on the Interconnectors and on the transmission network.

In making this decision the SEM Committee notes that one respondent argued that auctioning only capacity that is forecast to be available is discriminatory. This argument was made on the basis that where curtailment takes place under current practices, short-term traders are the worst affected because they already hold less capacity on the Interconnectors than longer term parties and in this instance, and less capacity is available for them to purchase. In this context, it is useful to note that Paragraph 2.6 of Annex I to Regulation (EC) No. 714/2009 states that:

“TSOs shall define an appropriate structure for the allocation of capacity between different timeframes. This may include an option for reserving a minimum percentage of interconnection capacity for daily or intra-daily allocation. Such an allocation structure shall be subject to review by the respective regulatory authorities. In drawing up their proposals, the TSOs shall take into account:

(a) the characteristics of the markets;

⁹ Regulation (EC) No. 714/2009, Annex I, Section 2.3

(b) the operational conditions, such as the implications of netting firmly declared schedules;

(c) the level of harmonisation of the percentages and timeframes adopted for the different capacity allocation mechanisms in place”.

Thus TSOs define an appropriate structure for the allocation of capacity between different timeframes. This structure is consulted upon by the Interconnector Owners from time to time. The practice will be further developed/ aligned in the Forwards Capacity Allocation Network Code. Therefore in the general course of auctioning capacity on interconnectors, there is no inconsistency between the Regulation and current practice.

However, the issue being dealt with here refers to what happens where there is a reduction in available capacity such as has been experienced on both the Moyle and EWIC in recent years.

In the event of unavailability, the Interconnector Owners cancel shorter term auctions in order to honour already allocated capacity contracts. The Interconnector Owners argue that this is not discriminatory because there is no actual capacity available to run short term auctions. One respondent in particular argued that this is discriminatory in that shorter term traders are being asked to shoulder the risk of outages.

On balance the SEM Committee agrees with the recommendation of the Interconnector Owners and so will not require any changes to be made to the Access Rules in relation to this specific issue. The reasons for this are as follows:

- There are effective congestion management procedures in place to ensure that any unused capacity is released to the market, thereby ensuring that no hoarding of capacity by long term capacity holders can occur.
- There is a secondary trading facility available for short-term traders to buy capacity from existing long-term holders if such trades are economic for the parties involved. Short-term users can also obtain capacity through UIOSI in the Access Rules and through the implicit auctions in SEM.
- It is important to maintain firmness of already allocated capacity. To move away from this could result in an unnecessary curtailment of allocated capacity.
- Other Interconnectors in the SEM and GB region adopt the same approach to auctioning capacity i.e. only capacity which is forecast to be available is auctioned. The SEM Committee believes that value can be placed on this regional alignment. In terms of attracting new players into the market, there is a value in having a coordinated approach to capacity auction management on different interconnectors within a region. A uniformity of approach may reduce barriers to trade as new participants do not need to familiarise themselves with different access rules on each interconnector they wish to trade on.

In summary, the SEM Committee's decision is that no change should be made to current practices by Interconnector Owners in managing auction capacity. However, as was suggested by the Interconnector Owners in their 5th April 2013 response, the SEM Committee request that the Access Arrangements make it explicit that where interconnector capacity is reduced that the reduced availability is spread pro-rata across all future auction volumes.

3. Capacity Curtailment Approach

3.1. Current practice

In situations where curtailment of sold capacity is required on the Moyle and EWIC (i.e. where the volume of capacity which has been sold in auctions is greater than the capacity that is available following an outage or a trip of an Interconnector) all capacity which has been sold is currently curtailed pro-rata and there is no differentiation made between longer term capacity holdings (e.g. annual) and shorter term capacity holdings (e.g. daily).

At the time of approving the Access Rules in 2012 the RAs requested that the interconnectors give further consideration to their curtailment practices. A Report on Curtailment Approach adopted on EWIC and Moyle was published on 13 November 2012 and the document elicited responses from market participants and stakeholders.

3.2. Summary of Responses

Responses on the capacity curtailment approach were submitted by six parties. Three of the respondents agreed with the current arrangements where curtailment was applied pro-rata and one of these three respondents in particular believed there was no just reason to discriminate between long and short term capacity holdings and that therefore the current arrangements were appropriate. All three stated that this may impact efficient cross-border trading in contravention of the EU Regulation.

Three additional respondents in contrast, would prefer to see the approach taken by the IFA implemented which favours long term capacity holders with capacity products curtailed in order from the shortest product duration to the longest. Two of these respondents supported their view by explaining that such an approach would reflect the long-term commercial commitment by parties that hold long-term capacity products.

3.3. Interconnector Owners' Recommendation

The Interconnector Owners noted that the respondents were split on the matter, where half of the respondents favoured an approach where capacity products are curtailed in order from the shortest product duration to the longest and the other half preferred a pro-rata curtailment approach where no differentiation is made regarding capacity products. The Interconnector Owners noted that a capacity right once nominated could be considered to hold the same value regardless of the timeframe it was bought in, despite their initial right to nominate having various values over time.

The Interconnector Owners are of the view that the current approach taken in the Access Rules is consistent with the Access Rules' objectives as set out in the respective interconnector operator licences, namely; offering available capacity, while ensuring transparency, objectivity and non-discrimination. Furthermore they argued that the

requirements of Annex I of Regulation (EC) 714/2009 have been objectively implemented in a non-discriminatory manner.

3.4.SEM Committee Decision

The SEM Committee is of the view that where curtailment of allocated capacity is required on the Moyle and EWIC (i.e. where the volume of capacity which has been sold in auctions is greater than the capacity that is available following an outage or a trip of an Interconnector), all capacity which has been allocated should be curtailed on a pro-rata basis. It should be noted that this approach to curtailment is consistent with the methodology employed by the BritNed Interconnector. The reasons for this decision are as follows:

- The SEM Committee believes that curtailment on a pro-rata basis is consistent with the Regulation which states that curtailment of capacity and transactions shall be applied in a non-discriminatory manner.
- This pro-rata approach is not discriminatory in that it does not distinguish between the treatment of the nominations of long-term capacity holdings and short-term capacity holdings.